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## Of Unrequited Deductions (and Lost Hopes)

by William T. Hutton

*The Back Forty* Chutzpah Award, bestowed at irregular intervals for breathtaking aspirations in income tax planning, goes this month to Grover and Mary Hope of Dallas, Texas. In 1984, the Hopes, dissatisfied with an administrative condemnation award attributable to the taking of their property for an extension of the Dallas North Tollway, decided to go to court.

In 1986, by judicial decree, their initial award of \$607,396 was amplified by an additional \$1,650,137. Happy ending? Might well have been, but for the fact that, against this discordant theme of condemnation and confrontation, the taxpayers heard a sweeter melody, the clinking of tax benefits. (Like a dog whistle, it may not have been audible to all listening ears.)

Specifically, the taxpayers alleged that they had made a charitable contribution to the Texas Turnpike Authority in the form of a bargain sale. Pursuant to their own \$4,038,623 estimate of value for the condemned property, they claimed a charitable contribution of \$1,781,089 (the approximate difference between the property's alleged fair market value and the total condemnation award). Not surprisingly, the IRS took exception to this treatment, disallowed the charitable deductions, which spanned three taxable years, and asserted liabilities for additional taxes, penalties, and interest of over \$1.4 million. The Hopes paid the assessed deficiencies, filed refund claims, and, upon IRS denial of those claims, took their case to the Claims Court.

It has been our belief that a charitable contribution could indeed be effected in the context of a condemnation proceeding. See *Herbert O. Robinson*, 33 T.C.M. 1140 (1974) (charitable deduction denied, but on finding that the value of the property did not exceed the condemnation award). If, for example, a landowner, aware of a legitimate threat of condemnation but prior to the instigation of proceedings, conveys the subject property to a land trust, there would seem to be no inherent inconsistency between the assertion of a charitable contribution deduction and the reinvestment of the bargain sale proceeds in qualifying replacement property (see IRC §1033). The amount of the charitable contribution would of course be subject to examination, as in any bargain sale case.

The claims court decision in *Hope*, rendered upon motion for summary judgment, was a complete victory for the Government, and forces us to reexamine our thinking about the condemnation/bargain sale transaction. The court was of "the opinion that a charitable contribution tax deduction should not be based on a completed condemnation proceeding, in which the state takes the land for a legitimate public purpose, and the landowner receives compensation...." The opinion seems grounded upon the finding that "just" compensation, as determined by the condemnation proceeding, firmly establishes the value of the property, leaving no room for the assertion of any bargain element. Thus, "once Grover Hope agreed to and was paid the compensation, he retained no further rights in the property." Or, to put it slightly differently, once Grover had settled with the state, the property's value was established for all collateral purposes. Thus interpreted, Grover Hope's travail ought not to be read as precluding the establishment of a charitable deduction on the transfer of property subject to threat of condemnation, so long as there has been no adjudication of property value in the state courts.

Whether or not other courts accept the Claims Court's categorical rule (no room for charitable deduction once adjudication has established the property's value), it is likely to prove exceedingly difficult to establish that a gift was intended once the taxpayer and the condemning authority have locked horns on the valuation issue. Message: Assess the contribution strategy as soon as awareness of the threat of condemnation arises, and involve a private charitable organization, the better to bolster evidence of "disinterested generosity".

*Hope v. U.S.*, U.S. Claims Court, 91 TNT 180-11 (August 28, 1991).